



**STATEMENT OF RUTH A. RITZEMA
SPECIAL AGENT IN CHARGE
NEW YORK FIELD OFFICE
OFFICE OF THE INSPECTOR GENERAL
U.S. DEPARTMENT OF HOUSING
AND URBAN DEVELOPMENT**

**BEFORE THE
HOUSE COMMITTEE ON HOMELAND SECURITY,
SUBCOMMITTEE ON MANAGEMENT,
INTEGRATION AND OVERSIGHT
UNITED STATES HOUSE OF REPRESENTATIVES**

JULY 13, 2006

Statement of Ruth Ritzema
Special Agent in Charge, New York Field Office
Office of the Inspector General
Department of Housing and Urban Development
Before the House Committee on Homeland Security,
Subcommittee on Management, Integration, and Oversight

Chairman Rogers, Ranking Member Meek, members of the Subcommittee; thank you for inviting me to testify today on the lessons learned after the events of September 11, 2001. Although this hearing is about the oversight efforts in fraud detection, prevention and control, which I will elaborate in great detail on, I wanted to start off my testimony by quickly sharing with you how the events of that day directly and intimately impacted me.

Events of September 11th

The Department of Housing and Urban Development's Office of Inspector General (HUD OIG) Office of Investigations, of which I am the Special Agent in Charge, was at 6 World Trade Center. It housed approximately thirty-five HUD OIG employees – special agents, forensic auditors and support staff.

On that morning, fortuitously, our New York City special agents were out of the office at a quarterly firearms qualification. Unfortunately, our forensic auditors and support staff were on site when the first plane hit the North Tower, which was adjacent to our office. All of the auditors and support staff in the building heard the explosion and one of our secretaries, who saw pieces of the plane and building fall, immediately told everyone to evacuate prior to any alarms going off. They fled across the street near the financial district where they watched the building burn. The group became separated when the second plane went into the South Tower.

Four of my special agents from our regional sub-office in Buffalo, New York, had flown in for their firearms qualification and they were to meet at our building at 9:00 a.m. for case reviews. The agents were traveling on the subway and made a lucky mistake by getting off at City Hall instead of the next exit that would have put them in the basement of the World Trade Center complex at exactly the wrong time.

I had meetings scheduled for that day in New Jersey and was across the river when I received a page from an agent about a fire at the World Trade Center. When I heard on the radio about the second plane going in, and worried about my own people, I immediately headed into the City using the shoulder of the New Jersey Turnpike to bypass the stopped traffic. As I approached the extension, I could see the towers on fire. I repeatedly tried to get through to headquarters, the staff or the offices, but as hard as I tried I only got a busy signal.

As I was driving towards the City, the first of the two towers collapsed before my eyes and I heard on the radio that the Pentagon had also been attacked. I drove through the Holland Tunnel

to the federal building located at 26 Federal Plaza, which is six blocks away from the World Trade Center and is also where the HUD OIG Office of Audit is located. A Federal Bureau of Investigations (FBI) agent told me that the emergency law enforcement command post was setting up at the church adjacent to the World Trade Center complex.

Running down Broadway, I was struck by how surreal the whole situation appeared. The beautiful cloudless day had turned all dark with soot and smoke in the air. People tried to turn me away from Ground Zero until I threw on my “Federal Agent” vest cover. I stopped from time to time to try to get help for a couple of people who had pretty serious burns. I then continued to run to the command post to check and make sure that our people were out safe. I just arrived at the church adjacent to the towers when the second tower collapsed literally right in front of me.

At that point, I have no memory of what happened during the collapse. My next memory is being about a block away with firemen all around and hearing screaming radio transmissions of firemen who were getting buried and were desperately trying to give their coordinates; “we’re at two o’clock from the fountain” (the fountain was located in the middle of the plaza). After the air cleared some, another FBI agent saw me and told me that we were rallying in Chinatown and he and I ran there.

I immediately agreed to work with and assist the FBI in any capacity. Our Assistant Special Agents in Charge (ASACs) had rallied our agents and were standing by for instruction. One of my ASAC’s and I went back to what was formerly our office and watched the building burn. Shortly thereafter, 7 World Trade Center collapsed. Training from my years in the military kicked in as we dispersed and established security perimeters to deal with the rumors and false reports swirling about in the dark mist of that day. Thankfully, and most importantly, we accounted for our people, but we had lost everything else – our evidence, all our case files, and our equipment. The HUD OIG had previously suffered a tragedy when one of our special agents died in the Oklahoma City bombing and I was very grateful how lucky we were considering our proximity to the devastation.

A command post was set up at 290 Broadway and it seemed that every law enforcement-related agency was in that room with a phone that rarely worked and a handwritten piece of paper taped in front of their table to identify their agency. Our OIG agents were stationed all over the city -- at command post, airports, Ground Zero or whatever other hot spot came up. They also searched for evidence with rakes, shovels and gloved hands at the landfill in Staten Island. This command post was move to the “Intrepid” in the Hudson River and to a garage on the West Side Highway where for the next few months our special agents continued to assist in the terrorist investigation and to transition back to HUD-related oversight activities.

Auditing Activities

In the aftermath, Congress authorized HUD to provide the State of New York with \$3.483 billion in Community Development Block Grant (CDBG) disaster assistance to aid recovery and revitalization and earmarked at least \$500 million of this to compensate small businesses,

nonprofit organizations, and individuals for economic losses. Out of these funds, the Empire State Development Corporation (ESDC), designated by New York State to develop and administer economic and business recovery grant and loan programs, was allocated \$700 million. The Lower Manhattan Development Corporation (LMDC), established to administer and develop programs to rebuild and revitalize lower Manhattan, was allocated \$2.783 billion.

Direction from the legislation insisted on speed in assisting businesses located in lower Manhattan hardest hit by the attack. For instance, applicants for Business Recovery Grants (BRG) were required to have a response to their request within 45 days of application submission. Congress also insisted on the utmost integrity from the program and required that the HUD OIG maintain a continuous audit activity of funds allocated to the rebuilding efforts. The Congress required that we report on the expenditure of the funds every six months. Our audit objectives to fulfill this mandate were to determine whether ESDC and LMDC:

- Disbursed the CDBG disaster funds to applicants in a timely manner;
- Disbursed the CDBG disaster funds to eligible applicants in accordance with HUD-approved action plans;
- Had financial management systems to adequately safeguard the funds; and
- Developed and implemented adequate procedures for monitoring the CDBG disaster assistance programs.

HUD OIG called for a meeting with Inspectors General from all the affected agencies to begin investigative and auditing coordination and cooperation in the New York/New Jersey office. Early collaboration with other agencies was important to the success of our auditing efforts. As a result, procedures were developed that provided that if an entity already received a Small Business Administration (SBA) grant and applied for a BRG grant, that entity could not receive a BRG grant if the total of both grants exceeded its economic loss. Likewise, we met with Federal Emergency Management Agency (FEMA) officials to also work on the issue of duplication of benefits among our programs.

We further collaborated with the Internal Revenue Service (IRS) to obtain a copy of an applicant's tax transcript, which was then used to verify that the tax information included on the application for computing economic loss was accurate. We discovered that some applicants did not file a tax return but still submitted a tax return on their BRG application and/or they sometimes included a higher taxable income than what was actually filed with the IRS in order to inflate economic loss. The auditors referred these over for investigation.

Additionally, we coordinated with the Social Security Administration (SSA) to test whether the social security numbers from our audit sample were legitimate. If our auditors discovered a discrepancy (i.e., the age of applicant did not agree with the age registered with the SSA), they referred it to investigations. In general, if the auditors detected any suspicious information during the course of its financial review, for instance, in the ESDC's Business Retention Grant (BRG) or Small Firm Attraction and Retention Grant (SFARG) programs or in the LMDC's Residential Grant program, it referred it to investigations for further review. This greatly enhanced anti-fraud and abuse endeavors.

HUD OIG auditors took a proactive approach that stressed prevention of fraud and abuse, as opposed to solely a detection emphasis whereby audits would take place long after the funds had been expended. The unusual nature of this audit recognized that the funds needed to be disbursed quickly and that Congress had waived the pre-set CDBG statutory requirements that governed the parameters of who were to receive grants. Early in the program our audits identified significant weaknesses in internal controls and program design. We conducted audits in an almost real-time basis that gave the auditee an early opportunity to take corrective action and improve controls and procedures for future expenditures. Audits were started no more than six months after the disbursements had been made. While this was resource intensive and caused a strain on our other operations as we had not been given any additional funds to undertake this initiative, we felt it was important that we remain aggressive and in the forefront.

To date, we have audited over \$1 billion dollars in disbursements. The results of these audits include findings of duplication of benefits and payments; of overpayments; of ineligible and unsupported costs, and of improvements needed in collection efforts. For example, our audit work found that over \$2 million had been disbursed to the Hudson River Park Improvements Program contrary to the terms of the sub-recipient agreement.

In furthering our early collaborative work with the SBA, only eight months after the attack, we issued an interim audit report noting the duplication of benefits between SBA loans and the ESDC's BRG program. We also reported on concerns we had with the calculation of recipients' economic loss amounts for the BRG program. As a response, ESDC developed procedures and formulas that tried to prevent duplication. ESDC also revised its application for the BRG program to require recipients to itemize the amount of claimed economic loss. In addition, it has responded by:

- Revising and enhancing controls and procedures to minimize ineligible and incorrect grant payments;
- Instituting additional efforts to collect grant overpayments;
- Hiring additional internal audit and investigative staff; and
- Establishing an audit staff of retired New York State Department of Public Service Commission employees to review the claims submitted by utility companies under the Utility Restoration and Infrastructure Rebuilding Program (i.e., they have completed audits of claims for two utility companies and disallowed in excess of \$33 million of the companies' \$99 million claim for reimbursement).

Investigative Activities

In addition to our audit work evaluating operational and administrative controls and other financial matters, we are also intensively involved in anti-fraud and abuse efforts. We have grouped our efforts into the three general areas of HUD expenses: immediate disaster relief funding, mid-term grant relief, and long term rebuilding expenditures. Our Office of Investigation works in cooperation with the Office of the United States Attorney to prosecute recipients that have fraudulently obtained CDBG funds. We have established working relationships with other federal agencies and State and city entities. Very early on, due in large

part to what our auditors were initially finding, we met with the U.S. Attorney's office to discuss the vulnerabilities and fraud patterns that were identified.

Originally established as an informal group by the U.S. Attorney's office, the World Trade Center Fraud Working Group solidified and began to meet monthly to discuss fraud concerns and share information on schemes. The working group was made up of high-level management that allowed for the discussion of complex matters and encouraged an environment where issues were expeditiously addressed. The working group attempted to, among other things, identify all the various agency dollars flowing into lower Manhattan, de-conflict cases, use automation to detect criminal activity, pass on criminal trends to enable better training, coordinate cases for maximum impact, identify legal weaknesses in the various programs and pass on recommendations to make them more fraud resistant, coordinate amnesty programs, and facilitate federal, State and local prosecutions.

This concentration of law enforcement and prosecutorial efforts resulted in the arrest and conviction of many perpetrators and also generated publicity that we believe had, to some extent, a deterrent effect. Members of the group included the:

- Office of the United States Attorney's-Southern District of New York
- Office of the Manhattan District Attorney
- Department of Labor-Office of Inspector General
- Department of Transportation-Office of Inspector General
- Federal Emergency and Management Agency-Office of Inspector General
- Small Business Administration-Office of Inspector General
- Social Security Administration-Office of the Inspector General
- Environmental Protection Agency-Office of Inspector General
- Internal Revenue Service – Criminal Investigation Division
- U.S. Postal Inspection Service
- New York City Department of Investigation
- Lower Manhattan Development Corporation
- State of New York- Office of Inspector General
- State of New York Insurance Department

Through our joint efforts, we have identified a number of types of potential criminal vulnerabilities that relate to the disaster assistance funding for lower Manhattan. These include:

1. False Statements and Claims
2. Wire Fraud
3. Mail Fraud
4. Theft or Bribery
5. Tax Evasion
6. Bid Rigging
7. Prevailing Wage Fraud
8. No Show Jobs
9. Artificial Price Market Inflation
10. Contract Fraud: Invoicing and Double Billing

11. Environmental Crimes
12. False Payrolls
13. Public Corruption
14. Embezzlement
15. Insurance Fraud
16. Collusion
17. Kickbacks

Every day our HUD OIG agents are at work on cases of fraud stemming from disaster funding for lower Manhattan. We received over 115 referrals as well as work we initiated. Although a number of our cases have been completed, we still have 62 cases open that are under investigation.

An example is the case against an individual who claimed his executive search firm sustained damage at 2 World Trade Center. He was convicted on 18 counts of defrauding nearly \$350,000 from private and government agencies of disaster benefits including grants and loans. FEMA, SBA, HUD and the Red Cross were among the targets of his fraud. Using forged documents, he received Business Recovery Grants for non-existent equipment that was supposedly lost when the tower collapsed.

In a further example, as I speak to you today, there is a trial that is proceeding against a man who submitted fraudulent applications to government programs, received \$118,000 that he was not entitled to, and applied for another grant when his scheme was uncovered. The amount of the grant award was calculated on the size of the business's expenses. So while his business was eligible for funds, he padded his application with thousands of dollars of phony expenses. He included lists of fake employees, business expenses, social security numbers, checks, wage reports that he supposedly filed with New York State -- but never did, lease agreements, and signatures that were forged onto other documents.

Another case involved a Maryland man, who was sentenced to 24 months incarceration, to 26 months of probation, was ordered to pay restitution of \$170,000, voluntarily forfeited \$280,000 to the government, and was fined \$10,200 for obtaining Business Recovery Grants claiming he had a business in lower Manhattan. In reality, the floor he claimed he was on was actually entirely occupied by a city agency. He offered a tax return that listed his business in lower Manhattan and reported gross earnings of \$3.3 million. Our investigation proved he had no business in lower Manhattan but worked from his home in Maryland and that the business reported minimal gross earnings.

Two other instances illustrate some of the early matters we were investigating. A New Jersey resident, who sublet his unit in lower Manhattan, fraudulently submitted a two-year commitment grant application, claiming he resided at his apartment on Pearl Street. A Manhattan woman claimed she lived on St. John Street and intended to stay in her apartment until the following year. In reality, she had moved uptown to W. 63rd Street. She had given LMDC a doctored lease and repeatedly lied about her address.

A case of public corruption was brought against an official of the New York State Division of Housing and Community Renewal. This official illegally obtained a LMDC Residential Retention Grant saying his father lived with him in lower Manhattan and he then sublet the unit at market rent prices.

Moreover, we found individuals who thought they would have easy access to money by establishing phony addresses. One such individual gave his address as 121 Reade Street, when in fact he lived further uptown on West 21st Street. This cost him a \$2,000 fine, 200 hours of community service and one year's probation.

The LMDC Residential Grant Program received more than 40,000 applications and distributed more than \$235 million. With each successful prosecution, we hoped that people who had lied to receive grant money had become anxious. To give these people a limited chance to come forward, a Fraudulent Grant Recipient Amnesty program was established. To date, over 160 households have returned money to the program.

Lessons Learned from September 11th Experiences

In addition to the establishment of a joint fraud working group, there are a number of initiatives that occurred, some of which we helped facilitate, which we believe are important to fraud detection, control and prevention.

A lower Manhattan Construction Command Center was organized to coordinate all construction valued at over \$25 million. As a result, a **Construction Integrity Team** was established which, among other things, consists of federal and local OIGs working in cooperation to evaluate vulnerabilities and improper activities. It has shared information so as to assist each of the contracting agencies in vetting contractors and subcontractors and to ensure the integrity of the process. It has set up an information campaign to deter fraudulent activity. It is also a productive venue to share facts on fraudulent and abusive trends. As construction and redevelopment begins, we anticipate that we will see more fraud and abuse involving contractors as HUD's funding moves away from benefit reimbursement to development efforts.

In order to provide a mechanism for the State and City to receive information on potential improper activity relating to construction, a **Fraud Prevention Hotline** was created under the direction and control of the Command Center. It was designed to receive allegations of corruption or criminal activity by any agency employee, public official, contractor employee, agent, subcontractor, vendor, or labor official. This hotline began operations in 2005. Posters publicizing the hotline are, and will be, located in all construction work sites and trailers. A press release was issued to inform the public. In addition, flyers are inserted in paychecks and stickers are placed on the back of employee identification cards in order to highlight the hotline's presence. Moreover, a website was created that contains a complaint form.

We also cooperated on a project that has established an employee **baseline background check** from third party databases that is overseen by a screening company. The background review will search for organized crime connections, terrorism ties, any previous histories of violence in construction, and theft and integrity issues. While recognizing that some employees involved in

construction may have had past criminal problems, this check will try to evaluate the nature of the crimes committed. It is important that the unions buy in to this process, as they did so with this project, or it will be very difficult to undertake.

Our oversight efforts have shown that the most effective way to proceed is to have monitoring be constant, continuous and at all the different levels of activity. **Monitors** should be concerned with: funds disbursement from the U.S. Treasury to State financial institutions; disbursements from the grantee to the sub-grantees; invoices and paperwork of the grantees and sub-grantees; timely reports for award and expenses; and timely reports on fraud prevention.

As I believe you have heard about in previous testimony, we also advocate the use of integrity monitors, also sometimes known as **Independent Private Sector Inspectors General (IPSIGs)**. These are monitors with legal, auditing, investigative and loss prevention skills that are employed usually by a government entity to ensure compliance with relevant laws, regulations and contracts. They can be helpful in the procurement or licensing phase of contracts and can assist in the vetting of initial contractors. In general, they act to deter, prevent, uncover and report unethical or illegal conduct that is especially useful if agency resources are inadequate to handle the response needed.

The HUD OIG labored to provide useful **fraud awareness training** to granting agencies. We gathered trends in criminal activity from a host of other law enforcement agencies in order to facilitate our training. We worked together with the ESDC and LMDC to train them on fraud detection techniques, particularly before grants were disbursed, as well as on identifying fraud indicators. This enabled the grantees to subsequently identify possible fraud and retain the necessary documentation for prosecution. We established a rapport that was designed to receive referrals from them on a timely basis. Although hard to measure, we believe these joint efforts helped to prevent, or to mitigate, a number of potential frauds as well as to uncover, and provide, evidence of criminal activity. We are currently working on a training module that will be geared to the contracting community as rebuilding efforts begin in earnest and that will include instruction in areas such as bribery awareness, false invoice detection, and bid rigging schemes. Throughout the grant implementation and distribution process, we continually educated the grantees on how to structure their application forms in a manner that would positively identify the applicant to reduce the potential for fraudulent applications and that would enumerate on the form the penalties for committing fraud.

From an auditing standpoint, we also believe there were important lessons learned. We believe it beneficial to: coordinate with other auditing entities to prevent overlap and duplication; hold meetings with auditees when new programs begin; utilize consultants or experts when necessary; use statistical sampling to better estimate results; discuss results early with auditees and local agency officials to prevent surprises; establish a relationship such that auditees will notify OIGs immediately upon the discovery of fraud; and work closely with investigators to get referrals to them quickly.

Oversight of Hurricane-related Disaster Relief Efforts

The destruction and aftermath of Hurricanes Katrina, Wilma and Rita challenge the HUD OIG with a task even more daunting than the reconstruction of lower Manhattan following the September 11th attack. Once again, an area of our nation has been hit by an unexpected disaster that has taxed emergency services and redirected federal Inspectors General toward assisting local government and overseeing the expenditure of a large amount of federal money. However, it also important to understand that there are differences, as they relate to our oversight efforts, between these two disasters.

From a HUD standpoint, New York City received approximately \$3.5 billion. At this juncture, the Gulf Coast States have received almost \$17 billion in assistance from HUD. With post-September 11th relief efforts: there were only two major “pass through” entities of CDBG funds; there were far fewer prospective grantees and sub-grantees, there was a limited land area to consider; and the oversight activities were, to some extent, more controllable. With the post-hurricane relief efforts: there is a multitude of “pass through” entities of CDBG funds in numerous States; there are thousands of grantees and sub-grantees; there is a huge land area of effected devastation; and, consequently, there is a much more arduous task for oversight.

Though we had some disaster experience with Hurricane Andrew in Florida a number of years back, we were definitely on a learning curve with our September 11th oversight activities. Each of our encounters have taught us some general lessons including probably the most important lesson -- that OIG teams on the ground, and at headquarters, must be proactive rather than reactive. This posture extends to collaboration. Joint task forces combine assets, manpower, information technology, budgets and other agency specialties to monitor expenditures and to attack fraudulent and criminal activities. To be truly effective, an OIG must continuously work to prevent waste, fraud and abuse by acting in real time and in a purposeful way to have a deterrent effect. Some of our best practices garnered from September 11th have become invaluable to us in this current effort. These include endeavors such as:

- Criminal investigators and auditors training State and local entities on how to uncover fraud, how to identify fraud indicators, how to retain necessary documentation; and how to make referrals to appropriate law enforcement;
- Participating in joint teams, such as grant fraud task forces and construction integrity teams;
- Setting up of hotlines and information campaigns on how to report fraud; and
- Properly vetting contractors and subcontractors and creating a clearinghouse database, as well as systems to conduct employee background checks.

In particular, we have especially honed our training capabilities over time and are providing in-depth and varied instructional opportunities on topics such as fraud detection in disaster relief settings to a host of entities in the effected Gulf Coast area. The first State to submit their plan was the State of Mississippi through their agency, the Mississippi Development Authority (MDA). The MDA met on several occasions with the HUD OIG to discuss their plan, listen to our concerns, and to be briefed by HUD OIG audit and investigative managers on the potential for scams and how to deal with application fraud, such as false statements, identity theft and false documents. In addition, as part of our fraud awareness efforts, the HUD OIG educated MDA contract appraisers hired to assess property damage on fraud red flags. Homeowners

applying for grant money received a HUD OIG fraud awareness bulletin as part of their application packet.

Though not the focus of this testimony, I would like to inform the Subcommittee that while we are working together to put controls in place we do, however, still have some concerns. From an audit oversight standpoint, the MDA plan, oversight and monitoring of grant funds ceases after the State has issued “compensation” funds to the homeowner “to be used at the discretion of the homeowner.” The MDA plan is concerned with the funds to the point when they are given to the homeowner, at which point they are allowed to work through their personal disaster recovery as they see fit. We do not think that monitoring and oversight should end at this phase and we have remaining concerns about how “compensation” plan that basically reimburses will spur the rebuilding of now blighted communities. What is to become of these communities in the future?

In general, our Office of Investigation down in the Gulf Coast region has created a far reaching fraud prevention program designed to: (1) create a training course for other agents/auditors and program officials to teach them to identify fraud specifically in CDBG programs; (2) sponsor fraud prevention meetings between HUD OIG and the major programs of HUD; and (3) sponsor fraud prevention meetings between the HUD OIG and industry groups such as the Mortgage Bankers Association, the Public Housing Authorities Directors Association; and the National Association of Housing and Redevelopment Officials.

As part of this prevention program, the HUD OIG also created a Suspicious Activity Report (SAR) that will be given to HUD grantees, sub-grantees, and others associated with delivering disaster funds. The SAR is a method of informing HUD OIG of suspected irregularities in the delivery of HUD program money.

Conclusion

In closing I would like to thank the Subcommittee for the opportunity to talk about the work that the agents, auditors, attorneys and support people of the HUD OIG have accomplished since the onset of this tragic and trying event. Our people do it because we are committed to the Department’s mission of providing safe, decent, sanitary and affordable housing for the Nation, and of providing economic development for our country’s communities. I look forward to answering questions that members may have.